R 5650-2

JAPAN · ECONOMIC · INSTITUTE

JEI REPORT

NO. 34B
September 19, 1986

IN THIS ISSUE:

Japan's Economy Bounces Back In Second Quarter 1

The Chips Are Down, But Prices Are Up 3

Trade Ministers Meet In Uruguay To Launch A New Round 5

California Amends Unitary Tax Statute 6

Election Concerns Shape Senate Action On Trade 7

Senate Democrats Announce Competitiveness Plan 8

Notes: Tobacco
Education Minister..... 10

Correction 10

Japan's Economy Bounces Back In Second Quarter

Led by personal consumption expenditures and housing investment, Japan's economy in the April-June quarter recovered from its January-March decline. Gross national product grew at an inflation-adjusted annual rate of 3.6 percent, compared to a 2.1 percent decline in the first three months of 1986 (see Table). The economy rose 0.9 percent with domestic demand accounting for 1.9 percentage points of growth and the external sector pushing it down by 1 percentage point.

Japan's Real Gross National Product at Constant (1980) Prices

(in billions of yen, seasonally adjusted, quarterly totals and rates of growth at annual rates)

	FY 1984	FY 1985	July-September 1985	October-December 1985	January-March 1986	April-June 1986
Gross National Product	Y281,102.2 (5.0%)	Y292,847.8 (4.2%)	Y291,379.9 (2.7%)	Y295,529.9 (5.8%)	Y293,979.6 (-2.1%)	Y296,621.7 (3.6%)
Personal Consumption Spending	159,100.7 (2.6%)	163,307.6 (2.6%)	162,777.8 (2.2%)	163,661.5 (2.2%)	164,664.0 (2.5%)	166,258.8 (3.9%)
Private Residential Construction	13,688.4 (0.4%)	14,197.8 (3.7%)	13,881.0 (-9.4%)	14,188.1 (9.1%)	14,539.1 (10.3%)	14,924.8 (11.0%)
Private Fixed Nonresidential Investment	47,342.6 (10.9%)	53,295.3 (12.6%)	52,981.2 (15.4%)	54,303.4 (10.4%)	54,492.2 (1.4%)	54,697.0 (1.5%)
Change in Business Inventories	1,839.1 (86.0%)	1,645.9 (-10.5%)	1,438.2 (-61.4%)	1,838.4 (167.0%)	1,504.3 (-55.2%)	656.9 (-96.4%)
Government Current Expenditures	26,654.9 (2.3%)	27,365.9 (2.7%)	27,192.9 (1.7%)	27,369.9 (2.6%)	27,819.7 (6.7%)	28,164.7 (5.1%)
Government Fixed Investment	22,159.9 (-3.0%)	20,637.9 (-6.9%)	20,495.6 (11.3%)	20,924.9 (8.6%)	20,782.0 (-2.7%)	21,522.2 (15.0%)
Change in Government Inventories	159.1 (*)	307.2 (*)	515.6 (*)	604.4 (*)	17.5 (*)	3,226.0 (*)
Net External Sector	10,157.3 (49.2%)	12,090.2 (19.0%)	12,097.6 (-30.6%)	12,639.3 (19.2%)	10,160.8 (-58.2%)	7,171.3 (-75.2%)
Exports of Goods and Services and Factor Income Received	53,609.8 (15.8%)	54,747.6 (2.1%)	55,077.6 (-13.9%)	54,720.5 (-2.6%)	51,844.6 (-19.4%)	52,754.6 (7.2%)
Imports of Goods and Services and Factor Income Paid	43,452.4 (10.0%)	42,657.4 (-1.8%)	42,980.0 (-8.3%)	42,081.2 (-8.1%)	41,683.8 (-3.7%)	45,583.3 (43.0%)

*Cannot be calculated or meaningless.

Source: Economic Planning Agency

Despite modest nominal wage increases, personal consumption spending rose at a 3.9 percent real annual pace in the second quarter. The relative stability of consumer prices strengthened households' purchasing power. The increase in private residential construction, sustained by low interest rates, remained in the 10 percent zone for the third consecutive quarter. Government spending also boosted the economy, in contrast to its negative contribution in FY 1985, with fixed investment and current expenditures in the April-June period (the first quarter of fiscal 1986) up at a 9.2 percent annual rate.

Despite the strength of domestic demand, the Economic Planning Agency predicted that the economy, which grew 4.2 percent in FY 1985, will be unable to achieve the 4 percent target set for the current fiscal year. Exports and business investment, the pillars of the economic expansion that began in March 1983, remain sluggish. Growth in private capital spending was under 2 percent for the second consecutive quarter as manufacturers scaled back investment plans in response to falling export volumes and profits. The external sector exerted a significant drag on the economy due to a 43 percent jump in imports. Tokyo's large purchases of gold to mint commemorative coins accounted for much of the rise, however, and explain the unusually large increase in government inventories.

The government has drawn up the outlines of the long-awaited economic stimulus package to be unveiled September 19. The program will include Y3 trillion ($19.4 billion at Y155=$1.00) of additional public works spending and Y500 billion ($3.2 billion) for other projects. The package, promised by the Liberal Democratic Party in the July election campaign, is one of the largest reflationary efforts ever undertaken by the government. Part of the package will be incorporated in the supplementary budget to be submitted to the Diet in mid-October. It is expected that the increased spending will be financed through the issue of construction bonds, although the Ministry of Finance has opposed increasing the government's debt burden.

Although the package also calls for flexible monetary policy, Bank of Japan governor Satoshi Sumita continues to state that he has no plans for a fourth cut in the official discount rate, which currently stands at 3.5 percent. The central bank chief, fearing a possible rekindling of inflation, has voiced concern over recent increases in land and stock prices. Finance Minister Kiichi Miyazawa, noting that the official discount rate is at a historically low level, stated that there is room for only one more cut. The interest rate on ordinary bank deposits is now set at a meager 0.38 percent. Extraordinary care must be taken, Mr. Miyazawa said, in the timing of the discount rate cut.

Randall S. Jones

The Chips Are Down, But Prices Are Up

The July 30 U.S.-Japan agreement on semiconductor trade has succeeded in one of its goals: Japanese makers of 256K and higher-density dynamic random-access memory (DRAM) chips are no longer selling their wares at bargain-basement prices. On the contrary, current prices are so high as to have a negative impact on both American and Japanese chip makers and distributors. The book-to-bill ratio, which compares the volume of new orders to shipments, fell below